

TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941

No. 248

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE, PETITIONER

vs.

LERNER STORES CORPORATION (MD.)

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED JULY 8, 1941
CERTIORARI GRANTED OCTOBER 13, 1941

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Before United States Board of Tax Appeals

Docket No. 99493

LERNER STORES CORPORATION (Md.), PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Docket entries

Appearances: For Petitioner: Andrew B. Trudgian, Esq. For Respondent: H. D. Thomas, Esq.

1939

July 11—Petition received and filed. Taxpayer notified. (Fee paid.)

July 11—Copy of petition served on general counsel.

July 28—Answer filed by general counsel.

July 28—Request for hearing in New York filed by general counsel.

Aug. 4—Notice issued placing proceeding on New York calendar—answer and request served.

1940

Apr. 4—Hearing set May 13, 1940, in New York City.

May 13—Hearing had before Mr. Leech on merits—submitted. Briefs due June 27, 1940—replies July 12, 1940.

May 23—Transcript of hearing 5/13/40 filed.

June 25—Motion for extension to July 6, 1940, to file brief filed by General Counsel. 6/27/40 granted as to both parties.

2 June 28—Brief filed by taxpayer. 7/5/40 copy served.

July 5—Brief filed by general counsel.

July 20—Reply brief filed by taxpayer.

Sept. 20—Memorandum findings of fact and opinion rendered—J. Russell Leech, Division 6. Decision will be entered for respondent.

Sept. 20—Decision entered—J. Russell Leech, Division 6.

Oct. 24—Stipulation of venue filed.

Oct. 24—Petition for review by U. S. Circuit Court of Appeals, Second Circuit, with assignments of error filed by taxpayer.

Oct. 24—Proof of service filed by taxpayer.

1940-

Nov. 6—Agreed praecipe for record filed with proof of service thereon.

Nov. 6—Notice of filing praecipe for record filed with proof of service thereon.

Before United States Board of Tax Appeals

Petition

Filed July 11, 1939

The above-named petitioner hereby petitions for a redetermination of the deficiency in excess-profits taxes set forth by the Commissioner of Internal Revenue in his notice of deficiency dated May 18, 1939, and as a basis of its proceeding, alleges as follows:

I

The petitioner is a corporation organized under the laws of the State of Maryland, with its principal office at 254 Fourth Avenue, New York, N. Y.

3

II

The notice of deficiency (a copy of which is attached and marked Exhibit A and made a part hereof), purports to have been mailed to the petitioner on May 18, 1939.

III

The taxes in controversy are excess-profits taxes in the amount of \$27,947.38 for the fiscal year ended January 31, 1937. Petitioner's return of income and excess-profits tax for the fiscal year ended January 31, 1937, was duly filed in the office of the Collector of Internal Revenue for the Third District of New York.

IV

The determination of excess-profits taxes set forth in the said notice of deficiency is based upon the following errors:

(a) In determining the net income, of the petitioner, subject to excess-profits tax for the fiscal year ended January 31, 1937, the Commissioner of Internal Revenue has erroneously failed or refused to allow as a deduction, therefrom, ten per cent of \$2,500,000.00, the corrected declared value of petitioner's capital stock as of June 30, 1936.

(b) The Commissioner has illegally and erroneously determined a deficiency in excess-profits taxes as due by petitioner for

the fiscal year ended January 31, 1937, under Section 106 of the Revenue Act of 1935, as amended by Section 402 of the Revenue Act of 1936, although these sections of law and the excess-profits tax imposed thereunder are invalid and unconstitutional under the Constitution of The United States of America.

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V

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

With respect to IV (a):

(a) In connection with the preparation of your petitioner's capital stock tax return for the capital stock tax year ending June 30, 1936, due consideration was given to all the factors involved in the determination of the value to be declared, and the decision was reached to declare the value of petitioner's entire capital stock in the amount of \$2,500,000.00. Despite the intention to establish a declared value of petitioner's capital stock in the amount of \$2,500,000, as the result of error and oversight in dropping two ciphers from the declared value which was to have been reported, a capital stock tax return was filed by your petitioner on September 26, 1936, incorrectly reflecting the declared value of its capital stock as \$25,000.00 instead of \$2,500,000.00.

(b) Prior to the annual closing of petitioner's books for the fiscal year ended January 31, 1937, the mistake made in filing a capital stock tax return indicating an erroneous declared value of \$25,000.00 instead of the correct declared value of \$2,500,000.00, which petitioner intended to declare, was discovered. Thereupon, on January 27, 1937, four days before the close of the petitioner's fiscal year, an amended capital stock tax return was duly filed with the Collector of Internal Revenue at Baltimore, Md., showing a declared value of \$2,500,000.00, in order to correct the mistake previously made in declaring an erroneous declared value of \$25,000.00 instead of \$2,500,000.00.

(c) On the income and excess-profits tax return filed by
5 your petitioner for the fiscal year ended January 31, 1937, the excess-profits tax liability for such period was computed upon the basis of using the corrected declared value of its capital stock, for the capital stock tax year ended June 30, 1936, in the amount of \$2,500,000.00, and upon such basis no liability for excess-profits tax was incurred.

(d) In computing the alleged deficiency in excess-profits tax the Commissioner of Internal Revenue used the incorrect declared value indicated on petitioner's original return of capital stock tax, for the capital stock tax year ended June 30, 1936, and upon such incorrect basis asserted the alleged deficiency in excess-profits tax in the amount of \$27,947.38.

With respect to IV (b):

(e) The Commissioner of Internal Revenue has determined excess-profits tax to be due by petitioner for the taxable year ended January 31, 1937 under Section 106 of the Revenue Act of 1935, as amended by Section 402 of the Revenue Act of 1936.

(f) Section 106 of the Revenue Act of 1935, as amended by Section 402 of the Revenue Act of 1936 imposed upon the net income of every corporation, for each income-tax taxable year ending after the close of the first year in respect of which it was taxable under Section 105 of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936, an excess-profits tax equivalent to the sum of the following:

“6 per centum of such portion of its net income for such income-tax taxable year as is in excess of 10 per centum and not in excess of 15 per centum of the adjusted declared value of capital stock;

12 per centum of such portion of its net income for such income-tax taxable year as is in excess of 15 per centum of the adjusted declared value of capital stock.”

The adjusted declared value of capital stock shall be determined as provided in Section 105 of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936, as of the close of the preceding income-tax taxable year (or as of the date of organization if it had no preceding income-tax taxable year).

(g) Section 105 of the Revenue Act of 1935, as amended by Section 401 of the Revenue Act of 1936, provided that for the first year ending June 30th, in respect of which the capital stock tax was imposed under Section 105, as amended, upon any corporation the adjusted declared value of capital stock shall be the value as declared by the corporation in its first return under Section 105, as amended, as of the close of its last income-tax taxable year ending at or prior to the close of the year for which the capital stock tax was imposed by Section 105, as amended.

(h) Under Sections 105 and 106, as amended, of the Revenue Act of 1935, the laying of the excess-profits tax provided for in Section 106, as amended, of the Revenue Act of 1935, was delegated to taxpayers. However, under Article 1, Section 8, of the Constitution of the United States, the Congress has the power to lay and collect taxes, duties, imposts and excises. Therefore, Section 106, as amended, of the Revenue Act of 1935, is unconstitutional, being in violation of Article 1, Section 8 of the Constitution of the United States. Further, Sections 105 and 106, as amended, of the Revenue Act of 1935 are unconstitutional, being in violation of the Fifth and Fourteenth Amendments of the Constitution of the United States in that Section 105, as amended, compels the payment of a tax based upon an arbitrary and unreasonable

7 amount not easily or accurately ascertainable nor defined within the law itself, nor based upon actual facts, but upon a basis prejudicial to petitioner by reason of its effect upon the tax imposed under Section 106, as amended, of the Revenue Act of 1935 resulting in the arbitrary deprivation or capricious confiscation of petitioner's property.

The petitioner keeps its accounts and renders its returns on the accrual basis of accounting.

Wherefore, the petitioner prays that this Board may hear the proceeding and find that the petitioner does not owe the alleged deficiency in excess-profits tax nor any part thereof asserted by the Commissioner of Internal Revenue in his notice of deficiency dated May 18, 1939; and the petitioner further prays that the Board may give and grant such other and further relief as in the premises the Board may deem fit and proper.

ANDREW B. TRUDGIAN,

Attorney for Petitioner,

125 Park Avenue, New York, N. Y.

(Verified by J. Henry Hersch, as Vice President, on July 10, 1939.)

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Exhibit A to Petition

[Copy]

TREASURY DEPARTMENT,

INTERNAL REVENUE SERVICE,

New York, N. Y., May 18, 1939.

Office of Internal Revenue Agent in Charge, U. S. Parcel Post Building, Upper New York Division

LERNER STORES CORPORATION (Md.),

354 Fourth Avenue, New York, New York.

SIRS: You are advised that the determination of your income tax liability for the taxable year ended January 31, 1937, discloses an overassessment of \$6,163.56 and that the determination of your excess-profits tax liability for the year mentioned discloses a deficiency of \$27,947.38 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiencies mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue

Agent in Charge, 341 Ninth Avenue, New York City, for the attention of Conf. CAC. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner,

By C. B. ALLEN,
Internal Revenue Agent in Charge.

STATEMENT

Lerner Stores Corporation (Md.), 354 Fourth Avenue, New York, N. Y.

Tax Liability for the Taxable Year Ended January 31, 1937

| | Liability | Assessed | Deficiency | Overassessment |
|-------------------------|-------------|-------------|-------------|----------------|
| Income Tax..... | \$41,193.75 | \$47,357.34 | | \$6,163.56 |
| Excess-profits tax..... | 27,947.38 | None | \$27,947.38 | |
| Totals..... | \$69,141.16 | \$47,357.34 | \$27,947.38 | \$6,163.56 |

In making this determination of your income tax and excess-profits tax liability, careful consideration has been given to the return filed by you and to the internal revenue agent's report transmitted to you by registered letter dated March 17, 1939, to which no reply has been received.

Adjustments to Net Income

| | |
|---|----------------|
| Net income as disclosed by return..... | \$1,666,300.27 |
| Unallowable deductions and additional income: | |
| (a) Capital stock taxes reduced..... | \$2,474.00 |
| (b) Depreciation..... | 208.72 |
| Net income adjusted..... | \$1,668,991.99 |

10

Explanation of Adjustments

- (a) You have been allowed a deduction of \$2,002.00 for capital-stock taxes accrued within the taxable year computed on the following basis:

| | |
|--|----------------|
| Declared value..... | \$25,000.00 |
| Plus: | |
| Income for year..... | 1,666,300.27 |
| Issue of Additional Capital Stock..... | 1,763,400.00 |
| Total..... | \$3,454,700.27 |
| Less: | |
| Dividend disbursement..... | 1,451,809.48 |
| Corrected Value..... | \$2,002,890.79 |

On a basis of \$1.00 per \$1,000.00, the proper accrual for capital-stock taxes amounts to \$2,002.00. Inasmuch as you claimed a deduction of \$4,476.00 the difference or \$2,474.00 has been disallowed.

(c) The depreciation deduction of \$9,564.58 as claimed by you has been decreased in the amount of \$208.72 based on the following schedule:

EXHIBIT B

| Furniture and fixtures | | Estimated useful life—10 years | | Adjusted life—10 years | |
|------------------------|---------------|--------------------------------|------------|------------------------|----------------------------|
| Year acquired | Original cost | Depreciation reserve | Balance | Remaining life | Depreciation for year |
| 1926..... | \$47,279.77 | \$39,133.66 | \$8,146.11 | 2 | A \$1,697.10 L 2,375.95 |
| 1927..... | | | | 3 | |
| 1928..... | | | | 4 | |
| 1929..... | 85,728.40 | 54,116.05 | 31,612.35 | 5 | A 2,634.38 L 3,688.00 |
| 1930..... | 40,518.50 | 21,058.66 | 19,459.84 | 6 | A 1,351.41 L 1,891.80 |
| 1931..... | 20,286.87 | 8,361.86 | 11,924.01 | 7 | A 710.37 L 994.49 |
| 11 1932..... | 8,131.90 | 2,571.97 | 5,559.93 | 8 | A 289.55 L 405.44 |
| | 291,964.44 | 125,242.20 | 76,712.24 | | A 6,662.81 L 9,355.86 |

A—Represents depreciation deducted by Associated Lerner Stores of America, Inc. to date of liquidation 2/1/36 to July 7, 1936.

L—Represents depreciation allowable to Lerner Stores Corp. (Maryland) from 7/1/36 to 1/31/1937.

Total depreciation claimed..... \$9,564.58

Total depreciation allowed..... 9,355.86

Depreciation disallowed..... \$208.72

The reduction of income taxes result from the allowance of the \$27,947.38 excess-profits tax, herein computed, as a credit against net income in computing the income tax liability.

You are liable for excess-profits taxes for the taxable year based on the original \$25,000.00 declared value as shown by your 1936 return of capital stock tax for the year ending June 30, 1936 in accordance with Section 106 of the Revenue Act of 1935 as amended by Section 402 of the Revenue Act of 1936; and Section 105 of the Revenue Act of 1935 as amended by section 401 of the Revenue Act of 1936. See also Chicago Telephone Supply Company vs. U. S., U. S. Ct. Cl. No. 43657, May 31, 1938, 23 F. Supp. 471, certiorari denied 10/10/38; and William A. Webster Co., Inc., 37 B. T. A. 800.

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Computation of Tax

Excess profits tax:

Taxable net income..... \$1,668,991.99

Less:

Dividends received credit (85% of
\$1,985,849.50)..... \$1,432,972.07

10% of \$25,000.00 value of capital stock
as declared in your capital stock tax
return for the year ended 6/30/36..... 2,500.00

1,435,472.07

Net income subject to excess profits tax..... \$233,519.92

5% of declared value of capital stock..... 1,250.00

Balance..... \$232,269.92

Excess profits tax:

6% of \$1,250.00..... 75.00

12% of \$232,269.92..... 27,872.38

Total excess profits tax..... 27,947.38

Excess profits tax assessed:

Original 1937 List Account No. 4-400008..... None

Deficiency of excess profits tax..... \$27,947.38

Income Tax:

Normal Tax:

Taxable net income..... \$1,668,991.99

Less:

Excess profits tax..... 27,947.38

Net income for Normal tax computation..... 1,641,044.61

13

Less:

85% of dividends received from taxable domestic
corporation..... 1,432,972.07

Normal tax net income..... \$208,072.54

8% of \$2,000.00..... 160.00

11% of \$13,000.00..... 1,430.00

13% of \$25,000.00..... 3,250.00

15% of \$168,072.54..... 25,210.88

Total Normal tax..... \$30,050.88

Surtax on Undistributed profits:

Taxable net income..... \$1,668,991.99

Less:

Excess profits taxes..... \$27,947.38

Normal tax..... 30,050.88

57,998.26

(a) Adjusted net income..... \$1,610,993.73

Less:

Dividends paid credit..... 1,451,809.48

(b) Undistributed net income..... 159,184.25

Less:

Specific credit..... None

Less—Continued.

| | |
|---|--------------|
| (c) Remainder subject to surtax..... | \$159,184.25 |
| 7% of \$159,184.25..... | 11,142.90 |
| Total surtax..... | 11,142.90 |
| Normal tax..... | 30,050.88 |
| Total income tax (Normal tax and surtax)..... | \$41,193.78 |
| Income tax assessed: | |
| Original 1937 list, Account No. 4-400008..... | 47,357.34 |
| Overassessment of income tax..... | \$6,163.56 |

14 Before United States Board of Tax Appeals

Answer

Filed July 28, 1939

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner, admits and denies as follows:

I. Admits the allegations contained in Paragraph I of the petition.

II. Admits the allegations contained in Paragraph II of the petition.

III. Admits that the taxes in controversy are excess profits taxes in the amount of \$27,947.38 for the fiscal year ended January 31, 1937. Denies that petitioner's return of income and excess profits tax for said fiscal year was filed in the office of the Collector of Internal Revenue for the Third District of New York.

IV. (a), (b). Denies that the respondent erred as alleged in sub-paragraphs (a) and (b) of Paragraph IV of the petition.

V. (a). Admits that a capital stock tax return was filed by petitioner on September 26, 1936, reflecting the declared value of its capital stock as \$25,000.00. Denies the remaining allegations contained in sub-paragraph (a) of Paragraph V of the petition.

(b), (c). Denies the allegations of fact contained in sub-paragraphs (b) and (c) of Paragraph V of the petition.

(d). Admits that in computing the deficiency in excess profits tax the Commissioner used the declared value of \$25,000.00 for the capital stock tax year ended June 30, 1936, but denies that he committed error in so doing. Denies the remaining allegations contained in sub-paragraph (d) of Paragraph V of the petition.

(e). Admits the allegations of fact contained in subparagraph (e) of Paragraph V of the petition.

(f), (g), (h). Denies the allegations of fact contained in subparagraphs (f), (g), and (h) of Paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and that petitioner's appeal be denied.

J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

E. O. HANSON,

Division Counsel.

HAROLD D. THOMAS,

Special Attorney, Bureau of Internal Revenue.

16 Before United States Board of Tax Appeals

Memorandum findings of fact and opinion

Sept. 20, 1940

Andrew B. Trudgian, Esq., for the petitioner.

H. D. Thomas, Esq., for the respondent.

LEECH: This is a proceeding to redetermine a deficiency of \$27,947.38 in excess-profits tax for the fiscal year ended January 31, 1937. Two issues are presented for decision. The first is whether petitioner is bound by its erroneous declaration of value on a capital stock tax return which was filed prior to the expiration of an extended period for filing such returns. The second question is whether the tax imposed by section 106 of the Revenue Act of 1935, as amended by the Revenue Act of 1936, is constitutional.

Findings of fact

Petitioner is a corporation organized under the laws of Maryland, with its principal offices in New York City, New York. It owns 52 subsidiary companies and its income consists of dividends from the latter.

Petitioner was granted an extension of time to September 29, 1936, within which to file its capital stock tax return for the year ended June 30, 1936. Pursuant to that extension, and on September 27, 1936, petitioner filed a capital stock tax return for the year ended June 30, 1936, in which it declared a value of \$25,000 for its capital stock. In the computation of tax on that return

the tax due was reported to be \$25 and the interest was reported as \$.25, making a total of \$25.25. The return was signed by J. H. Hersch and Graham Magee, both of whom were vice presidents of petitioner, and was duly sworn to by them under oath.

The figure of \$25,000 entered on the return was erroneous; the error arose through a mistake made by an employee of petitioner.

17 On January 27, 1937, petitioner forwarded a document prepared on Form 707 (the capital stock tax return form), which was stated to be an amended capital stock tax return for the year ending June 30, 1936. Under item 8 of this form, opposite the words "Declared Value of Entire Capital Stock," there was entered the figure of \$2,500,000. The amount of tax, penalty, and interest computed by petitioner on the form was \$3,090, consisting of a tax of \$2,500, a penalty of \$500, and interest of \$90.

The mistake in the first return was discovered by Hersch in the course of going over petitioner's accounts prior to the end of petitioner's fiscal year, which ended January 31, 1937.

By letter dated July 12, 1937, respondent advised petitioner that the declaration of value on the document sought to be filed as an amended return could not be accepted. The amount of money paid in connection with the so-called amended return was refunded to petitioner.

In computing the deduction of 10 per cent of the declared value in determining the net income of petitioner subject to excess-profits tax for the fiscal year ended January 31, 1937, respondent employed the declared value appearing on the first capital stock tax return, namely, \$25,000.

Opinion

Although we have found as a fact that the figure entered in petitioner's first return as the value of its capital stock was a mistake on the part of one of petitioner's employees, that finding is not particularly important to our disposition of this case, inasmuch as in these matters either a mistake or a change of mind has the same legal consequences.

The only question for a decision is whether petitioner may correct the error by filing an amended return after the period for filing the capital stock tax return has expired. This question has
18 been conclusively resolved against petitioner by the case of William B. Scaife & Sons Co., 41 B. T. A. 278. Furthermore, *Hagger Co. v. Helvering*, 308 U. S. 389, which is extensively relied upon by petitioner here, gives no support to petitioner's position, for the court goes no further there than to hold that a taxpayer may file an amendment to the first document he has filed

as a capital stock tax return within the time designated by statute for filing capital stock tax returns, or within such time thereafter as may be properly fixed by the Treasury. It does not hold that an amended return can successfully be filed after that period has run. See William B. Scaife & Sons Co., *supra*. We therefore resolve the first question against petitioner.

The next question is whether the excess-profits tax is constitutional. Petitioner attacks it on a number of grounds, but none of them seems to us to be any different than those advanced and passed upon adversely to petitioner in a number of cases which have sustained the excess-profits tax now before us or its earlier counterparts. *Chicago Telephone Supply Co. v. United States*, 23 Fed Supp. 471; cert. denied, 305 U. S. 628; *Patrick McGovern, Inc.*, 40 B. T. A. 705; *Allied Agents, Inc. v. United States*, 26 Fed. Supp. 98; cert. denied, 308 U. S. 561; *W. & K. Holding Corporation*, 38 B. T. A. 830; *Midvale Paper Board Co., Inc. v. United States*, 31 Fed. Supp. 851; *Mountain Iron Co. et al. v. United States*, 31 Fed. Supp. 895.

It is therefore our conclusion that respondent must be sustained on both issues.

Decision will be entered for the respondent.

Entered September 20, 1940.

————— [SEAL]

Decision

Entered Sept. 20, 1940

Pursuant to the determination of the Board, as set forth in its Memorandum Findings of Fact and Opinion entered September 20, 1940, it is

Ordered and decided: That there is a deficiency in excess-profits tax for the year ended January 31, 1937, in the amount of \$27,947.38.

Enter,

[SEAL]

(Signed) J. RUSSELL LEECH,

Member.

Before United States Board of Tax Appeals

Stipulation of venue

Filed Oct. 24, 1940

It is hereby stipulated and agreed by and between the parties to the above-entitled cause, by their respective undersigned at-

torneys, that the decision of the United States Board of Tax Appeals in said cause, dated September 20, 1940, and redetermining deficiency in Excess-Profits Taxes against the above-named petitioner for the fiscal year ended January 31, 1937, in the amount of \$27,947.38, may be reviewed by the United States Circuit Court of Appeals for the Second Circuit.

This agreement is made under and pursuant to the provisions of Section 1141 of the Internal Revenue Code.

Dated 23rd day of October, 1940.

ANDREW B. TRUDGIAN,
Attorney for Petitioner.
SAMUEL O. CLARK, Jr.,
Attorney for Respondent.

20 In United States Circuit Court of Appeals, Second
Circuit

Petition for review and assignment of errors

Filed Oct. 24, 1940

*To the Honorable, the Judges of the United States Circuit Court
of Appeals for the Second District:*

I

JURISDICTION

Lerner Stores Corporation (Md.), your petitioner, respectfully petitions this Honorable Court to review the decision of the United States Board of Tax Appeals entered on September 20, 1940, and finding a deficiency in Excess-Profits tax due from your petitioner for the fiscal year ended January 31, 1937, in the amount of \$27,947.38.

Your petitioner is a corporation organized under the laws of the State of Maryland, having its principal office and place of business at 354 Fourth Avenue, New York, N. Y.

On the 23rd day of October 1940, counsel for the petitioner and counsel for the Commissioner of Internal Revenue entered into a stipulation in writing under and pursuant to the provisions of Section 1141 of the Internal Revenue Code, wherein they designated the United States Circuit Court of Appeals for the Second Judicial Circuit as the appropriate Court to review the said decision of the United States Board of Tax Appeals.

Jurisdiction in this Court to review the decision of the United States Board of Tax Appeals aforesaid is founded upon Sections 1141 and 1142 of the Internal Revenue Code.

NATURE OF THE CONTROVERSY

The petitioner duly filed a Capital Stock Tax Return for the year ended June 30, 1936, showing a declared value as of January 31, 1936, in the amount of \$25,000.00. The officer supervising the filing of the Capital Stock Tax Returns for the petitioner and its fifty-two subsidiaries decided upon a declared value in the amount of \$2,500,000.00. However, through a clerical error on the part of a subordinate employee engaged in manually preparing the return, the \$25,000.00 figure was actually inserted on the return. Upon discovery of the error prior to the expiration of petitioner's fiscal year, on January 27, 1937, the petitioner filed an amended Capital Stock Tax Return showing the correct amount of \$2,500,000.00.

The Commissioner of Internal Revenue refused to accept the amended return, or to recognize the corrected declared value in the amount of \$2,500,000.00. In computing the ten per cent of the declared value as of January 31, 1936, allowed as a deduction in determining the amount of the net income of the petitioner subject to Excess-Profits tax for the fiscal year ended January 31, 1937, the Commissioner employed the declared value appearing on the first Capital Stock Tax Return, *viz*, \$25,000.00. This resulted in a deficiency of \$27,947.38 for the fiscal year ended January 31, 1937, as per the deficiency letter of the Commissioner of Internal Revenue dated May 18, 1939.

From this determination the petitioner appealed to the United States Board of Tax Appeals on July 11, 1939, assigning as error:

22 1—The refusal of the Commissioner to allow as a deduction, in determining the net income of the petitioner subject to Excess-Profits Tax, ten per cent of \$2,500,000.00, the corrected declared value as of January 31, 1936, appearing on the amended Capital Stock Tax Return;

2—The determination by the Commissioner of a deficiency in Excess-Profits Tax pursuant to the provisions of Section 106 of the Revenue Act of 1935, as amended by Section 402 of the Revenue Act of 1936, whereas those sections of law and the Excess-Profits Tax imposed thereunder are invalid and unconstitutional under the Constitution of the United States of America.

In a decision entered on September 20, 1940, the Board sustained the Commissioner on both points.

III

ASSIGNMENT OF ERRORS

In making its decision as aforesaid, the United States Board of Tax Appeals committed the following errors upon which your petitioner relies as the basis of its proceeding:

1—The Board erred in holding that, in determining the net income of the petitioner subject to **Excess-Profits Tax** for the fiscal year ended January 31, 1937, the declared value as of January 31, 1936, shall be the value inserted through clerical error of a subordinate employee on the first Capital Stock Tax Return filed for the year ended June 30, 1936, rather than the intended value appearing on the corrected Capital Stock Tax Return filed on January 27, 1937, prior to the close of the petitioner's fiscal year ending January 31, 1937.

2—The Board erred in holding that the **Excess-Profits tax**, imposed by Section 106 of the Revenue Act of 1935, as
23 amended by Section 402 of the Revenue Act of 1936, is valid and constitutional under the Constitution of the United States of America.

Wherefore, your petitioner prays that this Honorable Court may review the decision and order of the United States Board of Tax Appeals and reverse and set aside the same and direct the said Board to enter a decision and order that there is no deficiency in **Excess-Profits tax** for the fiscal year ended January 31, 1937; and for the entry of such further orders and directions as shall by this Court be deemed meet and proper, in accordance with law.

ANDREW B. TRUDGIAN,

Attorney for Petitioner,
125 Park Avenue, New York, N. Y.

(Verified October 21, 1940.)

In United States Circuit Court of Appeals

Notice of filing petition for review

Filed Oct. 24, 1940

To:

COMMISSIONER OF INTERNAL REVENUE,

Internal Revenue Building, Washington, D. C.

J. P. WENCHEL,

Attorney for Respondent,

Chief Counsel, Bureau of Internal Revenue,

Washington, D. C.

You are hereby notified that on the 24th day of October 1940
a petition for review by the United States Circuit Court of
24 Appeals for the Second Circuit of the decision of the United
States Board of Tax Appeals heretofore rendered in the
above-entitled cause, was filed with the Clerk of the Board. A
copy of the petition as filed is attached hereto and served upon you.
Dated October 24, 1940.

ANDREW B. TRUDGIAN,

Attorney for Petitioner,

125 Park Avenue, New York, N. Y.

Personal service of the foregoing notice, together with a copy of
the petition for review mentioned therein, is hereby acknowledged
this 24th day of October 1940.

J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue,

Attorney for Respondent.

Before United States Board of Tax Appeals

Praecipe for transcript

Filed Nov. 6, 1940

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit, and deliver to the Clerk of the
United States Circuit Court of Appeals for the Second Circuit,
copies duly certified as correct, the following documents and rec-
ords in the above-entitled cause in connection with the petition
for review by the said Circuit Court of Appeals for the Second
Circuit, heretofore filed by the above-named petitioner:

- 25 1—Docket entries of the proceedings before the Board.
 2—Petition for redetermination filed on July 11, 1939, together with annexed copy of deficiency letter.
 3—Answer of the respondent filed on July 28, 1939.
 4—Memorandum Finding of Facts and Opinion of the Board, promulgated September 20, 1940.
 5—Decision of the Board entered September 20, 1940.
 6—Petition for review filed on October 24, 1940.
 7—Notice of filing petition for review.
 8—This Praeceptum for record.
 9—Notice of filing this Praeceptum for record and the admission of service thereof.
 10—Stipulation designating the Circuit Court of Appeals for the Second Circuit as the appropriate court of review.
 Said transcript to be prepared as required by law and the rules of the United States Circuit Court of Appeals for the Second Circuit.

ANDREW B. TRUDGIAN,
Attorney for Petitioner.

Service of a copy of this praecipe is hereby admitted this 31st day of October, 1940.

Agreed to—

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue,
Attorney for Respondent.

26 Before United States Board of Tax Appeals

Notice of Filing of Praeceptum

Filed Nov. 6, 1940

To: Hon. J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, Internal Revenue Building, Washington, D. C.

Please take notice that on the 31st day of October, 1940, the undersigned, attorney for Lerner Stores Corporation (Md.), petitioner in the above-entitled proceeding, has filed with the Clerk of the United States Board of Tax Appeals a Praeceptum for Record, a copy of which is annexed hereto.

Dated October 31, 1940.

ANDREW B. TRUDGIAN,
Attorney for Petitioner.

Receipt of the foregoing notice of filing of the Praeipce for Record and service of a copy of the praecipe herein mentioned is acknowledged this 31st day of October, 1940.

J. P. WENCHEL,
Chief Counsel,
Bureau of Internal Revenue,
Attorney for Respondent.

27 [Clerk's Certificate to foregoing transcript omitted in printing.]

UNITED STATES CIRCUIT COURT OF APPEALS FOR
THE SECOND CIRCUIT

OCTOBER TERM, 1940

No. 188

(Decided March 24, 1941)

LERNER STORES CORPORATION (Md.), PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Petition to review a decision of the United States Board of Tax Appeals

The taxpayer seeks reversal of a decision of the Board which affirmed the commissioner's determination of a deficiency in the petitioner's excess profits tax for the fiscal year ending January 31, 1937.

Before SWAN, AUGUSTUS N. HAND and CHASE, *Circuit Judges*

SWAN, Circuit Judge: The tax in dispute is the petitioner's excess profits tax for the fiscal year 1937. Sections 105 and 106 of the Revenue Act of 1935, 49 Stat. 1017, as amended by sections 401 and 402 of the Revenue Act of 1936, 49 Stat. 1733, impose interrelated taxes on domestic corporations, namely a capital stock tax and an excess profits tax, calculated on the basis of the value of the capital stock as declared in the corporation's capital stock tax return for the first year in which the tax is imposed. The main question presented by the case at bar is whether a clerical error in the declared value of the capital stock as stated in a timely return may be corrected by filing a late amended return. To this question the Board of Tax Appeals gave a negative answer.

The facts as found by the Board are as follows: The petitioner is a corporation organized under the laws of Maryland, with its principal office in New York City. Its income is derived from dividends paid by subsidiary companies which it owns. Within the permitted time the petitioner filed a capital stock tax return for the first year ending June 30, 1936, in which the declared value of its capital stock was stated to be \$25,000. This figure was entered on the return in error, through a mistake made by an employee of the

petitioner. After discovering the error the petitioner, on January 27, 1937, forwarded to the commissioner what purported to be an amended capital stock tax return for the year ending June 30, 1936, in which the declared value of its capital stock was given as \$2,500,000, and payment was made of tax, penalty and interest computed on such amended return. On July 12, 1937, the commissioner advised the petitioner that the declaration of value on the document sought to be filed as an amended return could not be accepted. The money paid in connection with the so-called amended return was refunded to the petitioner. In determining the petitioner's net income subject to excess profits tax for the fiscal year ended January 31, 1937, the commissioner used the declared value of \$25,000 appearing on the first capital stock tax return. This resulted in the deficiency complained of. The Board sustained the commissioner, saying that although it had found as a fact that the figure of \$25,000 "was a mistake on the part of one of petitioner's employees," such finding was immaterial "inasmuch as in these matters either a mistake or a change of mind has the same legal consequences." The correctness of this ruling is the first question for consideration.

Section 105 (a) imposes on a domestic corporation an annual excise tax at the rate of "\$1 for each \$1,000 of the adjusted declared value of its capital stock." Section 105 (f) provides that "For the first year * * * the adjusted declared value shall be the value, as declared by the corporation in its first return under this section (which declaration of value cannot be amended), * * *." Despite this prohibition against amendment, a capital stock tax return may be amended within the time fixed for filing the first return. *Haggar Co. v. Helvering*, 308 U. S. 389. As Mr. Justice Stone there points out, at page 394, the purpose of the statute is to allow the taxpayer to fix for itself the taxable base for purposes of computation of the capital stock tax, but with the proviso that the amount thus fixed for the first taxable year shall be accepted for computing both capital stock and excess profits taxes in later years. It contemplates an exercise of judgment—"declaration of value"—by the taxpayer and a report of its decision in the return. Up to the time when the return is due, the taxpayer may change its judgment and report a higher value, as in the *Haggar* case; but a change of judgment thereafter cannot affect its taxes, for "the declaration of value cannot be amended." But we are not confronted with a change of judgment by the taxpayer; the case at bar presents a situation where the taxpayer has made but one "declaration of value" and has inaccurately reported it to the commissioner due to an error of one of its employees. The correction of such a clerical mistake before the commissioner has acted in reliance upon it in computing taxes for a later year cannot thwart the purposes of the statute or injure the interests of the government. The purpose of interlocking the excess profits tax with the capital stock tax was to induce corporations to exercise an honest judgment in declaring a fair or reasonable value

upon their stock. See *Glenn v. Oertel Co.*, 97 F. 2d 495, 496 (C. C. A. 6); *Rochester Gas & Electric Corp. v. McGowan*, 115 F. 2d 953, 954 (C. C. A. 2). The statute did not contemplate that the computation of the taxes would be based on clerical mistakes, and we can perceive no good reason for construing it to forbid their correction either before or after the return date, in the absence of facts raising an estoppel against the taxpayer. Suppose, for example, a corporation fails to file a capital stock return, or files one in which, through a typographical error, no figure whatever was inserted as the "declared value" of its stock. We cannot believe that a late return, in the first case, or an amended return, in the other, would not be received to enable the commissioner to assess the capital stock tax which the statute imposes. Cf. *Flomot Gin Co. v. Commissioner*, 40 B. T. A. 689. It is true that strict proof should be required to establish that the value stated in a return resulted from a clerical mistake; the amendment must not be used to substitute a declared valuation more favorable in the light of later events than the one originally decided upon and reported by the taxpayer. See *Riley Co. v. Commissioner*, 311 U. S. 55, 59. But granted that the valuation stated in the return was due to a clerical error, we think no sound reason can be advanced for not permitting it to be corrected before the commissioner has acted in reliance on it. Not to do so deprives the taxpayer of the privilege the statute accords to exercise its own judgment in fixing the taxable base.

The respondent cites *Riley Co. v. Commissioner*, 311 U. S. 55, as opposed to the conclusion we have reached. The statute there involved gave the taxpayer an election to take a percentage depletion allowance if he claimed it in his "first return." In ignorance of the statute, he failed to claim it originally but attempted to do so by an amended return. He was denied the right to do so; he elected too late. This case would be apposite if the petitioner at bar were attempting by amendment to change its judgment of the value to declare for its stock. It is not controlling where the amendment seeks to correct a clerical error in the return. Mr. Justice Douglas was careful to state at page 58, "We are not dealing with an amendment designed merely to correct errors and miscalculations in the original return. Admittedly the Treasury has been liberal in accepting such amended returns even though filed after the period for filing original returns." A case in the third circuit, *Wm. B. Scaife & Sons Co. v. Commissioner*, decided January 21, 1941, and not yet officially reported, supports the ruling of the Board. For the reasons already stated we respectfully disagree with it.

The petitioner attacks the constitutionality of the excess profits tax. This we ruled upon in *Rochester Gas & Electric Corp. v. McGowan*, 115 F. 2d 953, and are content to stand upon that opinion. Order reversed.

United States Circuit Court of Appeals, Second Circuit

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 12th day of April one thousand nine hundred and forty-one.

Present: HON. THOMAS W. SWAN, HON. AUGUSTUS N. HAND, HON. HARRIE B. CHASE, Circuit Judges.

LERNER STORES CORPORATION (Md.), PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the United States Board of Tax Appeals

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be and it hereby is reversed.

It is further ordered that a Mandate issue to the said Board in accordance with this decree.

D. E. ROBERTS, *Clerk*,
by A. M. BELL, *Deputy Clerk*.

Order for mandate—Filed Apr. 12, 1941—D. E. Roberts, Clerk.

UNITED STATES OF AMERICA,

Southern District of New York:

I, D. E. Roberts, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 34, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of Lerner Stores Corporation (Md.), Petitioner against Commissioner of Internal Revenue, Respondent, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this eleventh day of June, in the year of our Lord one thousand nine hundred and forty-one, and of the Independence of the said United States the one hundred and sixty-fifth.

[SEAL]

D. E. ROBERTS, *Clerk*.

Supreme Court of the United States

[Title omitted.]

Order allowing certiorari

Filed October 13, 1941

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.